

DOCKET FILE COPY ORIGINAL

RECEIVED

MAY 9 1994

FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of)
)
Price Cap Performance Review) CC Docket No. 94-1
for Local Exchange Carriers)

INITIAL COMMENTS OF
TIME WARNER COMMUNICATIONS

Of Counsel:
Paul B. Jones
Senior Vice President
Legal and Regulatory Affairs
Janis A. Stahlhut
Vice President
Regulatory Affairs
Time Warner Communications
300 First Stamford Place
Stamford, Connecticut 06902-6732

David R. Poe
Cherie R. Kiser
LeBoeuf, Lamb, Greene & MacRae
1875 Connecticut Avenue, N.W.
Washington, D.C. 20009-5728

Economic Consultants:
Susan M. Baldwin
Patricia D. Kravtin
Economics and Technology, Inc.
One Washington Mall
Boston, Massachusetts 02108

DATED: May 9, 1994

No. of Copies rec'd
List ABCDE

089

TABLE OF CONTENTS

SUMMARY	ii
I. Introduction	1
II. Goals and Context of the Commission's Price Cap Review	2
III. Relationship of Regulatory Changes to the Status of Competition	4
IV. Transition Issues	5
A. The state of competition for LEC local exchange and interstate access is such that there is no imminent need for a "transition" plan for LEC price caps.	5
B. While various regulatory and industry developments may have increased the prospects for competition in LEC-dominated access markets, they have not resulted in actual competition that can constrain the prices and behavior of LECs.	7
C. Objective criteria should be used to assess whether reduced or streamlined regulation should take effect.	11
D. LEC entry into related industries and markets has a substantial impact on the LEC price cap plan.	14
V. Because past predictions of the <i>pace of actual competitive development</i> in the telecommunications industry have been so imprecise, there is negligible value associated with attempting at this time to define the specific nature of regulatory reform for an unknown and <i>uncertain</i> future competitive environment.	15
VI. LECs should not be permitted to use the Commission's quality of service concerns as an excuse to implement infrastructure enhancements, network upgrades, and/or technological advancements that are actually intended for the delivery of future competitive services.	16
VII. The Commission should review LEC price caps again in three years.	17
VIII. Other Transition Issues	18
IX. Conclusion	20

SUMMARY

Time Warner, in its response to the Commission's *Notice of Proposed Rulemaking* regarding LEC price cap performance review, has focused its analysis on the goals of price cap regulation (particularly the goal of utilizing price cap regulation for purposes of developing a national telecommunications infrastructure) and the so-called "transition" issues. Time Warner is especially concerned that many of these transition matters presuppose a vision of competition that has not yet materialized, and which, if it occurs at all, is at best many years off. Inordinate focus upon specifics, that are by no means trivial, such as the criteria to be used to determine when to streamline regulation, revisions to baskets, etc., *before* effective competition has evolved, would be putting the cart before the horse. LECs have ample flexibility and earnings capabilities under the existing regulatory framework with which to position themselves in the current state of competitive development, *i.e.*, emerging competition. Based upon the current state of competition, there is no imminent need for any "transition plan" for LEC price caps.

The Commission's expectations regarding the development of competition for LEC access services are particularly troubling in light of recent initiatives by the Commission with respect to rate regulation of cable television providers who, if anyone, are most likely to be "competitors" of the LECs at some (as yet unknown) point in the future. Over the last year, the Commission has issued numerous rules

and regulations in the implementation of the *Cable Television Consumer Protection and Competition Act* ("Cable Act of 1992").*

While there may be disagreement as to the actual present extent of competition for LEC access services and the degree to which cable television service is itself monopolistic, it would be difficult to seriously contend that cable TV faces less competition than LEC access services. LECs control in excess of 99% of the access services market, while cable television competes with numerous close substitutes, including over-the-air broadcast television, video rental services, movies, live events and any number of other forms of entertainment. Providers of LEC basic access lines confront close to zero price elasticity whereas cable television service operators confront significantly greater price elasticity due to the fact that cable television consumers have a number of alternatives. If the Commission prematurely *relaxes* the regulation of LECs while imposing new and strict regulatory *constraints* upon the cable industry, the prospect of cable industry competition for LEC telecommunications markets is made even more remote than it has been up to now. Under the *status quo*, the earnings of cable firms are narrowly constrained, while the

* Pub. L. No. 102-385, 106 Stat. 1460 (1992). Some of the rules and regulations are detailed in *Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992, Report and Order and Further Notice of Proposed Rulemaking*, 8 FCC Rcd 5631 (1993); *First Order on Reconsideration, Second Report and Order, and Third Notice of Proposed Rulemaking*, 9 FCC Rcd 1164 (1993); *Second Order on Reconsideration, Fourth Report and Order and Fifth Notice of Proposed Rulemaking*, FCC MM Docket 92-266, FCC 94-38 (Released March 30, 1994); and *Report and Order and Further Notice of Proposed Rulemaking*, FCC MM Docket 93-215, FCC 94-39 (Released March 30, 1994).

price cap LECs undoubtedly will seek in this docket to enhance their earnings potential through the elimination of sharing mechanisms.

Although, since 1991, the Commission has made substantial headway in removing legal and operational barriers to LEC competitors, by any objective measure, actual or effective competition for LEC local exchange and access services does not presently exist, nor is it likely to exist for many years to come. The benefits of landmark events (such as the fact that tariffs for expanded interconnection have finally become effective although their lawfulness is still under investigation by the Commission and on appeal by the LECs) will not occur overnight. Moreover, no broad-based competition for interstate access services can possibly arise on a stand-alone basis without embracing jurisdictionally intrastate services as well. Hence, the actions of state regulators in removing barriers to local exchange competition are inextricably linked to the progress in competition for interstate access. For full competition to emerge for LEC switched access and local exchange service, alternative providers must be allowed to offer dial tone service (an option that is possible in only a handful of jurisdictions and has not yet occurred in any of them) and they must be actually in the business of offering service. Therefore, the Commission should evaluate the status of competition broadly and take no "transition" steps that in any sense assume or presuppose the presence or inevitability of competition for interstate access.

Time Warner urges the Commission to continue its various initiatives that will facilitate progress from today's LEC-dominated market to actual, effective competition. The establishment of just and reasonable rates for expanded

interconnection, the implementation of number portability, and progress with the advanced intelligent network proceedings are examples of specific ways that the Commission can ensure the steady progress toward effective competition. The adoption of unduly flexible pricing rules or overly generous price adjustment formulas that serve to buttress the already dominant LEC market power, as certain of the tentative conclusions set forth in the NPRM suggest the Commission may be considering, are more likely to hamper than stimulate the emergence of effective competition.

Before the
FEDERAL COMMUNICATIONS COMMISSION

RECEIVED

MAY 9 1994

Washington, D.C. 20554

FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

In the Matter of)
)
Price Cap Performance Review) CC Docket No. 94-1
for Local Exchange Carriers)

COMMENTS OF TIME WARNER COMMUNICATIONS

Time Warner Communications ("Time Warner"), pursuant to the Commission's *Public Notice*,¹ respectfully submits these initial comments on the price cap performance review for local exchange carriers.

I. Introduction

Time Warner is an emerging competitor of local exchange carriers ("LECs"), and thus has a strong interest in the evolution of the Commission's policies regarding the regulation of dominant carriers, the emergence of effective competition, and the development of an advanced national telecommunications infrastructure. The outcome of this proceeding regarding price caps for LECs will directly influence (1) Time Warner's ability to compete effectively with local exchange carriers and (2) Time Warner's ability to contribute to the development of a diverse, innovative, and reliable telecommunications network. A well-designed price cap plan will ensure that

¹ See, Order (DA 94-314) extending to May 9 and June 8 dates for filing comments and replies, respectively, In the Matter of Price Cap Performance Review for LECs, CC Docket No. 94-1, Order (released April 7, 1994).

LECs do not derive revenues from their noncompetitive services in excess of what they would derive in a fully competitive market, and will provide LECs and LECs' competitors with the appropriate incentives to build a modern telecommunications infrastructure that serves the public interest.

Time Warner fully supports the Commission's comprehensive efforts to evaluate whether price cap regulation is yielding the intended benefits and to modify that regulatory paradigm, as necessary, to ensure that the nation's telecommunications goals are being met in the most efficient manner possible. The Commission has encompassed "transition" issues within the scope of this proceeding, and specifically seeks comments on: the current state of competition; the impact of LECs' entry into related industries on the LEC price cap plan; and the relationship between price cap systems for LECs and the development of the nation's infrastructure.²

In the comments that follows, Time Warner addresses first the goals and context of the Commission's review of LEC price caps; second, the relationship of regulatory changes to the status of competition; and third (and in the most detail), the transitional issues identified in the NPRM.

II. Goals and Context of the Commission's Price Cap Review

The Commission, in conducting its comprehensive review of LEC price caps, should consider carefully the context of the review. Of particular significance are the following characteristics of today's telecommunications market for services provided by LECs:

² NPRM, para. 92 through 100.

- Competitors have not yet made effective inroads into LEC markets.
- LECs are eager to make substantial inroads into new lines of business.
- The LECs control essential bottleneck network capabilities upon which their competitors depend.
- Although the Commission is making commendable progress in addressing them, numerous, formidable barriers continue to prevent the development of effective competition.

The Commission seeks to shape "the LEC price cap plan to play its part in setting regulatory policies to assure that the bright potential offered us by modern telecommunications becomes a reality."³ The likelihood of the country achieving the Commission's goal depends greatly upon the degree to which LEC competitors can successfully enter and serve telecommunications markets. Therefore, in its deliberation of the multiple and complex issues in this proceeding, the Commission should reject the erroneous assumption that the country should rely exclusively (or even primarily) on LECs to fulfill important national telecommunications goals. The most appropriate vision of the future is one in which all suppliers (LECs and LECs' competitors) contribute to the development of a national information infrastructure in a way that is efficient and fair.

The LECs' unique control over essential bottleneck capabilities upon which customers and competitors depend, clearly and substantially differentiates the price cap regulation of LECs from the price cap regulation of AT&T. Therefore, the path followed in upcoming years by the Commission as it continues to modify LEC price cap regulation to reflect changes in the telecommunications industry will, of necessity, diverge from the path followed by the Commission in its price cap regulation of

³ NPRM, para. 8.

AT&T. The barriers that prevented other companies from competing effectively with AT&T have been eliminated; indeed, they had largely disappeared before price caps were implemented for AT&T. Furthermore, AT&T does not control network capabilities upon which MCI, Sprint, and other competitive interexchange carriers rely.⁴ In stark contrast, numerous barriers continue to prevent the development of effective competition with local exchange carriers *and* LECs' competitors are forced to depend upon the LECs' network capabilities in order to provide telecommunications services. As a result, the pricing flexibility afforded LECs under price caps should reflect this substantial difference between them and AT&T.

III. Relationship of Regulatory Changes to the Status of Competition.

Changes in regulatory framework cannot be equated to actual changes in the marketplace in which LEC services are sold and bought. Less than one year has passed since the LECs' interstate expanded interconnection tariffs for special access became effective and the analogous tariffs for switched transport became effective only three months ago.⁵ Although the implementation of these tariffs represents an important milestone, as is discussed below, the LECs continue to dominate the

⁴ For example, equal access in LEC central offices has been implemented and 800 number portability is now available.

⁵ *See, Expanded Interconnection with Local Telephone Company Facilities, Report and Order and Notice of Proposed Rulemaking*, 7 FCC Rcd 7369 (1992) (*Special Access Order*); *Expanded Interconnection with Local Telephone Company Facilities*, CC Docket No. 91-141 (Phase I) and *Amendment of Part 36 of the Commission's Rules and Establishment of a Joint Board*, CC Docket No. 80-286, Second Report and Order and Third Notice of Proposed Rulemaking, 8 FCC Rcd 7374 (1993) (*Switched Access Order*); *Expanded Interconnection with Local Telephone Company Facilities*, Second Memorandum Opinion and Order on Reconsideration, 8 FCC Rcd 7341 (1993) (*Special Access Second Reconsideration Order*).

interstate access market. Moreover, as also shown below, there are still non-trivial regulatory hurdles that are preventing the development of competition.

Therefore, the timely elimination of barriers to competition is a subject warranting the Commission's focused examination. Furthermore, although many of the Commission's actions (external to the price cap proceeding) are facilitating the development of competition, there is a vast difference between the *possibility* of competition (which can be enhanced through bold regulatory initiatives) and the *actual* presence of carriers actively competing in the market.

Price caps were developed as a regulatory alternative designed to eliminate some of the inherent inefficiencies in rate of return regulation. While price caps generally were intended to encourage behavior among LECs that would more closely than rate of return regulation replicate the discipline of a competitive market, the effect of price caps on the emergence of competition was never empirically examined. This now needs to be done. The Commission should not assume that any aspect of price caps has a benign effect on the development of competition in LEC markets. The convergence of diverse regulatory developments (decisions that are enhancing new entrants' ability to compete in the LECs' traditional markets, and decisions that are enabling LECs to pursue new, nontraditional lines of business) will continue to influence the prospects for competition in the local exchange and access markets. Consequently, the Commission should consider not only the impact of emerging competition on LEC price caps, but, more importantly, the impact of LEC price caps on the prospects for competition.

IV. Transition Issues

- A. The state of competition for LEC local exchange and interstate access is such that there is no imminent need for a "transition" plan for LEC price caps.**

The Commission seeks comments on numerous "transition issues" for the purpose of developing "data and information relevant to fashioning a workable plan for revising the baseline price cap model as competition develops."⁶ Significantly, and quite appropriately, the Commission has proposed no specific transition plan for LEC price caps at the present time.⁷ The Commission has concluded, not unreasonably, that "for the price cap LECs, technological changes and Commission decisions such as the requirement that the LECs provide expanded interconnection of their facilities with competitors *have laid a foundation for competition* in the market for local exchange access services."⁸ However, given the embryonic state of competition for LEC local exchange and interstate access services, there is no imminent need for a "transition plan" for LEC price caps.

Moreover, adoption of a "transition" policy that favors LECs, by providing them with even greater flexibility and the ability to increase profit levels at the expense of captive ratepayers, would have a chilling effect on both emerging competition in local exchange and interstate access service markets now overwhelmingly dominated by the LECs, but also competition in the new markets (*i.e.*, cable TV, inter-LATA toll,) that LECs are now actively seeking to enter.

In order to provide consumers with the "full benefits of competition" in telecommunications markets, the Commission should first ensure that the baseline

⁶ NPRM, para. 94.

⁷ *Id.*

⁸ *Id.*, para. 93, *emphasis added*.

price caps model for LECs is consistent with its pro-competitive goals. Second, the Commission should adopt criteria for determining whether effective competition exists for local exchange and interstate access service markets that are sufficiently rigorous so as to provide necessary protection for both customers and competitors of price cap LECs.⁹

B. While various regulatory and industry developments may have increased the prospects for competition in LEC-dominated access markets, they have not resulted in actual competition that can constrain the prices and behavior of LECs.

In Transition Issue 1a, the FCC requests comment on the current state of competition in providing local exchange and interstate access, and the most relevant and useful criteria for determining when to adopt streamlined regulation and data relevant to such criteria.

The Commission acknowledges that the LECs currently dominate the provision of access services.¹⁰ The Commission further expresses the view, however, that "increased competition within local exchange areas now seems inevitable, even if the level of competition that will result cannot be predicted with any certainty and may differ where local market conditions differ."¹¹ Indeed, Commission-mandated interconnection requirements, the expansion of alternative access provider services, the growing use of wireless services (cellular, and in the future, PCS) to provide radio links between end users and LEC and IXC switches, the potential of cable television systems (over time and with substantial investment) to offer an alternative

⁹ *Id.*, para. 95.

¹⁰ *Id.*

¹¹ *Id.*

to the LEC "local loop" as the link between the customer and the LEC switch, and alliances between traditional telecommunications carriers and potential future alternative local service providers, have all contributed to a *perception* that competition in local exchange and interstate access services markets has either already arrived or is just around the corner. The fact is, however, that while these developments may have increased the prospects for competition in LEC-dominated access markets, they have not resulted in actual competition of a magnitude sufficient to constrain the prices and behavior of LECs. The ubiquity of LEC networks, the enormous investments required to build alternative local networks across the country, the time it will take to win customers away from the incumbents, and the power of the dominant LECs to thwart competitive entry ensure that effective competition will take many, many years to develop.

The limits of competition in access markets today can be observed both empirically and analytically. An examination of current market conditions unambiguously confirms the sheer absence of competition operating at a level that is sufficient to constrain the market power of the dominant LECs. Moreover, the present lack of competition beyond specialized niche market segments is likely to persist for many years, if not indefinitely, due to the presence of formidable *economic* barriers to competitive entry that result from financial and market resources that are and that continue to be uniquely available to the LECs.

A number of key factors demonstrate the limits of competition in LEC markets today, and the resources available to the LECs to maintain their bottleneck control for quite some time:

- (1) *Alternative access providers have captured a very small portion of the market.* Aggregate revenues, which are paid by long distance carriers and end users, for access services of all

Competitive Access Providers ("CAPs") combined are approximately \$220 million, or *less than one percent* of the \$26 billion LEC access services market.¹² Capital investment for the CAPS as of 1993 was approximately \$1.13 billion as compared with \$201 billion in LEC gross plant in service as of 1993.¹³ CAP employees number in the vicinity of 3,000, as compared with over 500,000 for the LECs.¹⁴ That CAPs may be efficient providers of geographically-specialized, high-volume services does not diminish the monopoly position of the LECs in markets where the LECs are most efficient: the provision of ubiquitous switched access connections to more than 100 million individual residential and business subscribers.

(2) *The LECs' ability to continue to earn substantial revenues and profits on terminating access remains totally unchallenged by any CAP or other competitor.* Even large business customers that can efficiently utilize LEC special access or CAP services must rely on LEC switched access to terminate their traffic.

(3) *Wireless services are not substitutes for local service today.*

The costs, capacity constraints, quality and reliability of wireless services relative to basic local service preclude direct substitution. In addition, the vast majority of cellular calls

¹² Source of CAP data is the 1993 ALT Report, Connecticut Research Report: Competitive Telecommunications by Connecticut Research, Vol. I, No. 1, January 1, 1994 ("1993 ALT Report"). Sources of the LEC data are the Form M Annual Reports and 10K Reports.

¹³ *Id.*

¹⁴ *Id.*

ultimately involve landline connections, so that cellular is not an alternate to LEC access, but rather a complement to LEC landline services.

- (4) *Significant legal barriers to competition exist.* Without concurrent authority, albeit under state jurisdiction, to provision switched dial tone services, full competition for LEC switched access will not emerge. It is simply not economically feasible to invest in switching capability for one without the other. Today, only a handful of states have granted switched dial tone authority and there is little if any measurable switched dial tone service being offered by alternative providers.
- (5) *Cable companies have yet to make competitive inroads into local telephone service.* Cable systems require substantial capital investments to provide two-way telephony. In view of the investments required and the reality of regulatory impediments at the local level, it may be some time before any significant number of consumers would have a competitive alternative available, even under the most favorable scenarios.
- (6) *LEC revenues account for more than 99% of the relevant local telecommunications market.* Total LEC revenues for all core local telecommunications services were \$97.4-billion in 1993,¹⁵ whereas total revenues for all non-LEC providers of local telecommunications services combined was only \$347-million.¹⁶

¹⁵ 10K Annual Reports (for RBHCs), Value Line (for other LECs). Core local telecommunications services consist of residential and business local exchange access line services, carrier access services, local calling, intraLATA long distance calling, and local/intraLATA private line services.

¹⁶ 1993 ALT Report, supra n. 12.

- (7) *LECs are able to generate substantial cash flow through depreciation charges against regulated telecommunications services.* At the present time, the LECs control in excess of \$201-billion in gross rate base assets subject to regulation at the federal and state levels.¹⁷ These assets have a net book value of \$121.3-billion.¹⁸ In 1993, the LECs took depreciation expenses against rate base assets totalling in excess of \$14-billion.¹⁹ The LECs have regularly sought and have regularly received authority for increases in annual depreciation rates at the federal and state levels. Extrapolating from recent experience and trends, it is likely that between now and the year 2000, the LECs will generate roughly *\$100-billion* as a result of depreciation charges relating to regulated core telecommunications services, creating cash flow for reinvestment at a level that dwarfs all of the potential competitors combined.

Thus, while it is true that competition is likely to increase for telecommunications services over the next five to ten years under appropriate regulatory and market conditions, the level and scope of competitive entry is unlikely to be sufficient to eliminate or even reduce the market power of the LECs. Considerable time is required for effective and sustainable competition to emerge in LEC-dominated access markets. Indeed, the final phases (including tariffing) of the Commission's expanded interconnection investigation and rulemaking are far from

¹⁷ 10K Reports and Form M for all RBHCs, 1984-1993.

¹⁸ 10K Reports for all RBHCs, 1993.

¹⁹ *Id.*

completed, and interconnection barriers are just beginning to be reduced. Lessons can be learned from the customer premises and long distance markets: it can take years, if not decades, for effective competition to develop even in the face of pro-competitive policies and initiatives. The market for local exchange and interstate access services is presently at an extremely early stage of the transition to competition. One of the worst things the Commission could do from the standpoint of promoting a successful transition to competition is to prematurely relax LEC price cap rules.

C. Objective criteria should be used to assess whether reduced or streamlined regulation should take effect.

In Transition Issue 1b, the Commission identifies numerous criteria to be used for determining when reduced or streamlined regulation for price cap LECs should take effect. These criteria include:

- (1) the nature and extent of any barriers to market entry and exit (*e.g.*, regulatory, economic, or technological obstacles); (2) the existence of potential and actual competitors and, if so, what role should the existence of potential and actual competition play in determining whether to reduce or streamline LEC price cap regulation; (3) the extent to which those competitors have the facilities to serve LEC customers; (4) the willingness of customers to use competitors' services and, if so, how should this criterion be measured; (5) the competitors' market share and, if so, how should the term "market" be define; (6) pricing trends; (7) the effect of expanded interconnection; (8) differences in competition in different geographic locations or regions, and differences in demographic characteristics, such as whether services

are available to all groups within a broad community or area; or (9) other factors.²⁰

Time Warner cautions against reliance on criteria nos. 2, 3, and 4, in particular, that might be satisfied by vague, qualitative, or anecdotal showings of potential competition, the mere existence of competitors, or perceived willingness of customers to use competitors' services. Structural measures for determining effective competition, including measures of actual competition in geographical markets, market share,²¹ interconnection in LEC central offices, and barriers to entry,²² such as reflected in criteria nos. 1, 5, and 7, provide much more meaningful and robust criteria.

In addition, some other factors which would be appropriate as criteria for determining effective competition include:

- (1) *Functional Equivalency of Competitive Offerings.* Functionally equivalent service or services are offered and generally available from at least one supplier other than the dominant LEC within the same geographic area in which a customer resides and in which the LEC is

²⁰ NPRM, para. 95.

²¹ In measuring market share, revenue-weighted output is preferable to a quantity metric (e.g., minutes), where different products are involved, because revenue weighting appropriately reflects the relative value of each product line. The dedicated access services typically furnished by CAPs are substantially different from the switched access services furnished by LECs and indeed LECs are themselves in the dedicated ("special") access business.

²² Barriers to entry could be in the form of legal, regulatory, technological or economic conditions. Such barriers could appear in the form of franchise requirements, easements or rights-of-way, pre-qualification financial requirements, or exceptionally high start-up costs, for example.

providing service,²³ and the service must be competitively available with the same degree of ubiquity throughout the LEC's service territory.²⁴

- (2) *Substitutability of Competitive Offerings in the Presence of Multiple Competing Suppliers.* Reasonable substitutes for the service are offered and generally available from more than one supplier other than the dominant LEC within the same geographic area²⁵ in which a customer resides and the LEC is providing service, and the service must be competitively available with the same degree of ubiquity throughout the LEC's service territory.²⁶

²³ "Functional equivalency" means that the competitively-supplied service is technically capable of providing the same function as the service furnished by the telecommunications utility and that it is likely to be perceived as similar or identical by a customer. Furthermore, the customer must be able to take the functionally equivalent service within the same geographic market area, i.e., without moving the location at which the service is to be provided.

²⁴ Ubiquity of availability is particularly relevant in the case of network services, because the presence of geographically selective competition would afford the dominant telecommunications utility the ability to leverage its ubiquity in the noncompetitive regions of its service territory into geographic areas in which competition may be locally present. The ubiquity requirement may, however, be satisfied if the dominant telecommunications utility affords the competing nondominant firm(s) and/or its(their) customers the *unimpeded ability* for the services of such competing firm(s) to be interconnected with the services offered by the dominant telecommunications utility through co-location in its central offices.

²⁵ The customer must be able to take the functionally equivalent service within the same geographic market area, i.e., without moving the location at which the service is to be provided.

²⁶ Where multiple suppliers of competing services are present, the ubiquity requirement may be satisfied if the dominant telecommunications utility shall afford the competing nondominant firm(s) and/or its(their) customers the *unimpeded ability* (e.g., co-location in its central offices) for the services of such competing firm(s) to be interconnected with the services offered by the dominant telecommunications utility or the *unimpeded ability* for the services of the several firms to be interconnected

(continued...)

- (3) *Not an Essential or Bottleneck Service.* The service proposed for reclassification must not be an essential or bottleneck facility whose use is required by a provider of a competing service. In other words, the service must not be an input for the provision of a competitive service for which there are either no functionally equivalent services or for which multiple other suppliers do not exist.

As an alternative to the consideration of the numerous structural criteria identified above, the Commission could instead rely upon an all-encompassing criterion, which can be characterized as a "*Stand-Alone Test*." Under the "stand alone test" *a service could be classified as competitive only if its functions could still be furnished by other providers even if the telephone company itself did not offer the service.* Clearly, under these circumstances, a LEC would no longer control essential "bottleneck" facilities for the service, the point to be addressed under Transition Issue 1c.

D. LEC entry into related industries and markets has a substantial impact on the LEC price cap plan.

The importance of maintaining (or narrowing) the flexibility afforded LECs by the price cap model is even more critical in Transition Issue 1c, which considers the possibility of LEC entry into related markets such as cable TV and inter-LATA toll. Clearly, if LECs are provided with even greater flexibility and the ability to increase profit levels even further at the expense of captive ratepayers, competitors in the related markets would be placed at an enormous disadvantage, and the Commission's

²⁶(...continued)

with one another and with the services offered by the dominant telecommunications utility.

objective of robust facilities-based competition in these markets would be in jeopardy. Thus, the fact that LECs are actively seeking entry into related industries and markets *strengthens* - not weakens - the importance of at least maintaining LEC price cap rules as they presently exist.

Because the Commission is seeking to apply a fairly stringent standard of rate regulation on the cable TV industry, it would be particularly inappropriate for the Commission to loosen controls even further for the LECs. As widely recognized, both LECs and cable TV companies are positioned to bring modern telecommunications infrastructure to a broad base of consumers. The Commission must take extreme care that it does not unfairly handicap one potential competitor, either through the regulation imposed directly on that competitor or indirectly through premature relaxation of regulation on the other competitor.

- V. **Because past predictions of the *pace of actual competitive development* in the telecommunications industry have been imprecise, there is negligible value associated with attempting at this time to define the specific nature of regulatory reform for an unknown and *uncertain* future competitive environment.**

In Transition Issues 2 and 3, the Notice of Proposed Rulemaking ("NPRM") solicits comments on future adjustments to price cap regulation, or the adoption of some other form of streamlined regulation, as LEC services become subject to greater competition. The Commission suggests several possibilities, including widening the price cap bands, moving specific baskets or services out of price caps, and reducing tariff filing requirements. The Commission also asks whether it is appropriate to *schedule* revisions in the composition of price cap baskets or adopt procedures that would rebalance baskets in response to specified conditions in market conditions.

The perception that competition is *almost* at hand has been with us for most of the last ten years,²⁷ but progress has been slow, sporadic and by no means inexorable. In this proceeding, the Commission is taking its first comprehensive look at the price cap plans in light of recent historical experience and expectations for the foreseeable future. Because past predictions of the *pace of actual competitive development* in the telecommunications industry have been so imprecise, Time Warner questions the value of attempting at this time to define the specific nature of regulatory reform for an unknown and *uncertain* future competitive environment.

Any attempt to predict and anticipate the course of competitive developments more than several years away will lead to unproductive speculation. Deferring further re-evaluation and adjustment of LEC regulation until such time as additional facts and experience are available makes more sense.

VI. LECs should not be permitted to use the Commission's quality of service concerns as an excuse to implement infrastructure enhancements, network upgrades, and/or technological advancements that are actually intended for the delivery of future competitive services.

In Transition Issue 4, the NPRM seeks comment on "whether and how the Commission should revise its monitoring of LEC service quality, network reliability, and infrastructure as part of any transition plan."²⁸ The Commission expresses concern that differing levels of service quality will be provided by the LECs in their

²⁷ This figure is derived by using as measures such seminal events as Divestiture (1984) and the decision in Computer Inquiry III to adopt Open Network Architecture requirements (1985). However, the time since federal and state regulators first set in place policies aimed at promoting competition in the telecommunications is more like *a quarter of a century*, using as benchmarks the FCC's Above 790 (1959) and Carterphone (1968) decisions.

²⁸ NPRM, para 98.

various services areas based upon the degree of competition and the relative level (or lack) of affluence of the customers. Under this scenario, some areas and some customer groups would enjoy higher quality of service than would others.

Time Warner fully supports the Commission's efforts toward ensuring adequate, reliable service for all customer groups and for all parts of the country. However, the Commission, in addressing these legitimate concerns, should retain a healthy degree of skepticism regarding LEC invocation of the service quality mantra as an excuse to implement infrastructure enhancements, network upgrades, and/or technological advancements that are actually intended for delivery of future competitive services. The LECs should be held to strict quality of service standards, but plans for relaxed regulation relating to infrastructure enhancements and upgrades should not escape scrutiny because they are packaged as quality of service improvements.

VII. The Commission should review LEC price caps again in three years.

In Transition Issue 5, the Commission requests comment on the frequency of review of the LEC price cap plan mechanism.²⁹ The Commission states that "[o]ur approach to keep abreast of the transitional regulatory changes that might be needed in the years ahead might be to review the LEC price cap plan more often than every fourth year."³⁰ The Commission also indicates that more frequent reviews may raise other concerns, including administrative burdens and states that, in the alternative, Commission monitoring may be a solution.³¹

²⁹ NPRM, para 99.

³⁰ *Id.*

³¹ *Id.*

The Commission is clearly correct in concluding that the timing of the review of the LEC price cap plan needs to carefully balance conflicting goals. Frequent re-evaluation of the parameters would largely defeat the purpose of alternative regulation, while infrequent reviews could facilitate monopoly abuses and excessive price levels. If the price cap mechanism and monitoring requirements are properly set at the outset, excessively frequent review would be inappropriate, and, furthermore could dampen any LEC incentives for innovation, and cost-cutting strategies. Also, continual review, as noted by the Commission, would be burdensome not only to the Commission, but also to interested parties. A price cap mechanism, if appropriately structured, should govern itself over a set period.

A three-year interval will provide a sufficiently long term for the revised price cap mechanism to be tested and to evaluate the impact of the price cap plan on the emergence of competition. Furthermore, a review in no more than three years is essential to ensure that the price cap plan is successfully simulating a competitive market.

VIII. Other Transition Issues

In Transition Issue 6, the Commission invites parties to comment on "whether and how the Commission should adopt changes in rules and policies other than those specifically mentioned" in the NPRM as part of a transition plan for LEC price caps.³² The Commission recognizes (correctly) the fact that many decisions that it will make between when the plan is revised in this proceeding and when the plan will be reviewed again, may affect the workings of the price cap plan. It is imperative, however, that future Commission decisions not be hindered by the revised LEC price

³² NPRM, para. 100.